

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

December 17, 2002

IN RE:

**BELLSOUTH TELECOMMUNICATIONS, INC.
COMPUTATION OF PRICE REGULATION
INDEX AND SERVICE PRICE INDEX**

**DOCKET NO.
02-00513**

**ORDER APPROVING PRICE REGULATION FILING
BY BELLSOUTH TELECOMMUNICATIONS, INC.**

This matter came before Directors Deborah Taylor Tate, Pat Miller and Ron Jones of the Tennessee Regulatory Authority (the "Authority" or "TRA"), the voting panel assigned to this docket, at the regularly scheduled Authority Conference held on August 19, 2002, for consideration of BellSouth Telecommunications, Inc.'s ("BellSouth") Computation of Price Regulation Index and Service Price Index filing.

Background

BellSouth filed its original application to operate under price regulation pursuant to Tenn. Code Ann. § 65-5-209 with the Tennessee Public Service Commission (the "TPSC") on June 20, 1995.¹ The TPSC's January 23, 1996 Order implementing BellSouth's price regulation plan also required BellSouth to reduce its rates by approximately 56.3 million dollars. BellSouth filed a petition for review of the TPSC's Order, and through decisions and orders issued on October 1, 1997 and November 19, 1997, the Tennessee Court of Appeals vacated the TPSC's January 23,

¹ BellSouth's application was filed in TPSC Docket No. 95-02614, which after remand from the Court of Appeals became TRA Docket No. 95-02614.

1996 Order. Thereafter, on October 27, 1998, the Authority deliberated on BellSouth's application for a price regulation plan and approved BellSouth's price regulation application with an effective date of October 1, 1995. The Authority's *Order Approving BellSouth's Telecommunications, Inc.'s Application for Approving BellSouth Telecommunications, Inc.'s Application for Price Regulation Plan*, entered on December 9, 1998, set forth the following provisions for BellSouth's price regulation plan:

Increases in BellSouth's initial rates for Basic Local Exchange Telephone Service shall not occur until December 1, 2002, consistent with Tenn. Code Ann. § 65-5-209(f).

Increases in BellSouth's rates for Call Waiting shall not occur until December 1, 2002, consistent with Tenn. Code Ann. § 65-5-209(h).

Annual adjustments in BellSouth's basic and nonbasic rates pursuant to Tenn. Code Ann. § 65-5-209(e) shall be calculated from December 1, 1998, and the calculation of the Service Price Index for basic and nonbasic services shall be based upon service volumes for the month of December for the year of the annual filing and upon service prices in effect on December 1, 1998 or as reset by the Authority under Tenn. Code Ann. § 65-5-207.

Annual adjustments in BellSouth rates for Interconnection Services pursuant to Tenn. Code Ann. § 65-5-209(g) shall be calculated from December 1, 1998.²

The Authority's December 9, 1998 Order also provided that BellSouth's price regulation plan would be subject to the price regulation methodology stipulated to in *In Re: United Telephone Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423.³

² *In Re: Application of BellSouth Telecommunications, Inc. for a Price-Regulation Plan*, Docket No. 95-02614, *Order Approving BellSouth Telecommunications, Inc.'s Application for Approving BellSouth's Telecommunications, Inc.'s Application for Price Regulation Plan*, 21 (December 9, 1998).

³ See *In Re: United Telephone-Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423, *Order Approving in Part and Denying in Part Tariff No. 96-201* (September 4, 1997).

The Consumer Advocate Division of the Office of Attorney General filed a Petition for Review in the Tennessee Court of Appeals on February 9, 1999, seeking a reversal of the Authority's December 9, 1998 Order. The Court of Appeals affirmed the Authority's Order in an opinion issued on January 10, 2000.

BellSouth's June 26, 2000 Filing

On June 26, 2000, BellSouth submitted to the Authority its first filing pursuant to its price regulation plan, consisting of calculations of its December 1, 1999 Price Regulation Index ("PRI") and Service Price Index ("SPI") pursuant to Tenn. Code Ann. § 65-5-209. BellSouth's filing included 911 Emergency Services, ESSX Station Lines, MultiServ Plus Station Lines, Centrex Station Lines, and Basic Rate ISDN (integrated services digital network) services in the non-basic services category in calculating the PRI and SPI, even though the Authority had previously determined that such services should be categorized as basic local exchange telephone services ("basic services").⁴ The Authority found that classifying these services as non-basic would result in a distortion of the price cap calculations. Accordingly, the Authority required BellSouth to refile its price regulation filing, reclassifying 911 Emergency Services, ESSX Station Lines, MultiServ Plus Station Lines, Centrex Station Lines and Basic Rate ISDN calculation as basic services. On December 4, 2000, BellSouth filed a revised computation of

⁴ "Basic local exchange telephone services" and "non-basic services" are defined in Tenn. Code Ann. § 65-5-208(a). Tenn. Code Ann. § 65-5-209(f) provides that "the initial basic local exchange telephone service rates of an incumbent local exchange telephone company shall not increase for a period of four (4) years from the date the incumbent local exchange telephone company becomes subject to such regulation." This initial four-year freeze does not apply to rates for non-basic services, which may be increased as long as such increase complies with the formula set forth in Tenn. Code Ann. § 65-5-208(e). In an Order issued on November 30, 1998, in Docket No. 97-01438, the Authority determined that ISDN should be classified as a basic service under Tenn. Code Ann. § 65-5-208(a)(1). See *In Re: UTSE Tariff No. 97-361 to Reflect the 1997 Price Cap Adjustment*, Docket No. 97-01438, Order Denying Tariff No. 97-361 (November 30, 1998). On March 20, 2001, the Tennessee Court of Appeals issued a decision reversing the Authority's November 30, 1998 Order and holding that ISDN is a non-basic service. See *United Telephone-Southeast, Inc. v. Tennessee Regulatory Authority*, No. M1999-02801-COA-R12-CV, 2001 WL 266051 (Tenn. App. March 20, 2001) (permission to appeal to Tennessee Supreme Court denied September 10, 2001).

the December 1, 1999 PRI and SPI, wherein BellSouth reclassified and modified its categorization of basic and non-basic services to address the Authority's concerns and to reflect prior decisions of the Authority.⁵

At the January 9, 2001 Authority Conference, after review of the revised filing and the supporting information, the Authority determined that BellSouth's PRI and SPI for non-basic services had been calculated in accordance with Tenn. Code Ann. § 65-5-209 and the methodology approved by the Authority, including all orders issued concerning United Telephone-Southeast's prior price regulation filings.⁶ Moreover, the Authority found that BellSouth's current prices for non-basic services were less than the maximum prices allowed under Tenn. Code Ann. § 65-5-209, thereby creating headroom within which future rate increases might be made. According to the PRI and SPI, BellSouth had approximately 18.2 million dollars in available headroom for rates in its non-basic services category.⁷ Based on these findings, the Authority approved the non-basic SPI and PRI calculations in BellSouth's December 4, 2000 price regulation filing. The Authority denied approval of the SPI and PRI indexes for basic services, having found that such services are subject to the four-year price freeze set forth in Tenn. Code Ann. § 65-5-209(f) and the indexes for those services are to be established at the end of the four (4) year price freeze.⁸

⁵ The revised filing also complied with the Authority's decision in Docket No. 00-00863, in which the ESSX intercom rate element, ESSX ISDN, and Centrex ISDN were ruled basic services. *See In Re: BellSouth Telecommunications, Inc. Tariff to Increase ESSX, Digital ESSX, and ESSX ISDN Rates*, Docket No. 00-00863, *Order Denying Tariff* (April 26, 2001).

⁶ *See Consumer Advocate Division v. Tennessee Regulatory Authority*, No. M1999-01699-COA-R12-CV, 2000 WL 1514324 (Tenn. App. Oct. 12, 2000) (Discussing price regulation methodology).

⁷ Headroom represents the difference between actual aggregate revenues and aggregate revenues allowable under the formula set forth in Tenn. Code Ann. § 65-5-209(e). In this instance, headroom had been created primarily due to access reductions which had been partially offset by rate increases to Complete Choice Service and various custom calling services. BellSouth did not propose to change any basic or non-basic rates in this filing.

⁸ *See In Re: BellSouth Telecommunications, Inc. Computation of Price Regulation Index and Service Price Index*, Docket No. 00-00545, *Order Approving Price Regulation Filing by BellSouth Telecommunications, Inc.* (December 18, 2001).

BellSouth's May 6, 2002 Price Regulation Filing

BellSouth filed its 2001 Price Regulation Plan, which is the subject of this docket, on May 6, 2002. This filing contains BellSouth's calculations of its 2001 PRI and SPI pursuant to Tenn. Code Ann. § 65-5-209 and the price cap methodology approved by this Authority. It covers the period from December 2000 to December 2001. No rate changes are being proposed in this filing.

Findings and Conclusions

After analyzing the overall price cap filing, the Authority finds that BellSouth's PRI and SPI indices for non-basic services have been calculated in accordance with Tenn. Code Ann. § 65-5-209 and the methodology approved by the Authority, including all orders issued concerning BellSouth's price cap filings in prior years, with one (1) exception. BellSouth proposes that Centrex Service previously classified by the Authority as a basic service should be reclassified as a non-basic service, in light of the Court of Appeals' decision in *United Telephone-Southeast, Inc. v. Tennessee Regulatory Authority*, No. M1999-02801-COA-R12-CV, 2001 WL 266051 (Tenn. App. March 20, 2001).

As stated above, pursuant to Tenn. Code. Ann. § 65-5-208, the telecommunications services of price-regulated carriers must be classified as either basic or non-basic. In its September 4, 1997 Order in Docket No. 96-01423, the Authority ruled that the station lines for United Telephone-Southeast, Inc.'s ("UTSE") Advanced Business Connection Service ("ABC Service"), including associated network access registers, are basic services.⁹ The functionality of

⁹ In re: *United Telephone-Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423, *Order Approving in Part and Denying in Part Tariff No. 96-201* (September 4, 1997).

UTSE's ABC Service is essentially equivalent to BellSouth's Centrex (or ESSX) Service.¹⁰ Because of the Authority's 1997 decision regarding ABC Service and the high degree of similarity between ABC Service and Centrex Service, the Authority previously ruled that BellSouth's Centrex Service is a basic service.¹¹

In March 2001, the Tennessee Court of Appeals issued its opinion in *United Telephone-Southeast, Inc. v. Tennessee Regulatory Authority*.¹² In that case the Court reviewed the Authority's decision to classify ISDN as a basic service pursuant to Tenn. Code Ann. § 65-5-208(a). The Court concluded "that the legislature intended that 'basic' services have some correlation to 'essential' services."¹³ The Court further held that ISDN is not a basic service because "ISDN provides more than basic or fundamental telephone communications . . . [and] nothing . . . supports a conclusion that this functionality is critical to the average telephone consumer."¹⁴

The pertinent part of Tenn. Code Ann. § 65-5-208(a)(1) defines "basic local exchange telephone services" as comprising "an access line, dial tone, touch-tone and usage provided to the premises for the provision of two-way switched voice or data transmission." All other services are defined as non-basic services.¹⁵ The Court of Appeals' ISDN decision provides the necessary guidelines for analyzing whether a service should be classified as basic or non-basic. Notwithstanding the Authority's previous rulings classifying the station lines of ABC Service

¹⁰ The terms "Centrex" and "ESSX" are interchangeable. BellSouth Centrex service is a central office-based business service designed to serve customers having communications characteristics such as multi-location, need for frequent and convenient interconnection services, and unpredictable growth requiring flexibility and expandability.

¹¹ *In re BellSouth Telecommunications, Inc. Tariff to Increase ESSX, Digital ESSX and ESSX ISDN Rates*, Docket No. 00-00863, *Order Denying Tariff* (April 26, 2001).

¹² *United Telephone-Southeast, Inc. v. Tennessee Regulatory Authority*, No. M1999-02801-COA-R12-CV, 2001 WL 266051 (Tenn. Ct. App. March 20, 2001) (permission to appeal to Tennessee Supreme Court denied September 10, 2001).

¹³ *Id.*, at *3.

¹⁴ *Id.*, at *6.

¹⁵ Tenn. Code Ann. § 65-5-208(a)(2).

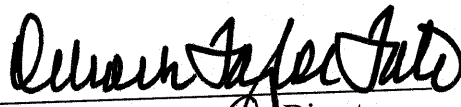
and Centrex Service as basic services, the Authority finds that Centrex should be classified as a non-basic service based on the criteria established in the Court of Appeals' opinion and pursuant to Tenn. Code Ann. § 65-5-208(a)(2).


Taking this change into consideration, the Authority's review indicates that BellSouth's current prices for non-basic services are less than the maximum prices for non-basic services allowed under Tenn. Code Ann. § 65-5-209, thus creating headroom for which future rate increases may be made. The Authority has determined that BellSouth has approximately 5.8 million dollars in available headroom for its non-basic services.

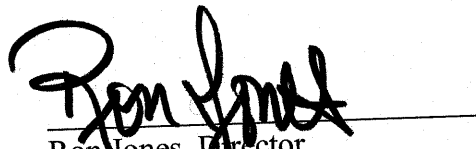
Upon careful review of BellSouth's computation of its Price Regulation Index and Service Price Index filing for non-basic services, and of the entire record in this matter, the voting panel voted unanimously to approve BellSouth's filing.

IT IS THEREFORE ORDERED THAT:

1. Centrex Service shall be classified as a non-basic telecommunications service pursuant to Tenn. Code Ann. § 65-5-208(a)(2).
2. BellSouth's Computation of its Price Regulation Index and Service Price Index for non-basic services, filed on May 3, 2002, is approved.


Deborah Taylor Tate, Director


Pat Miller, Director


Ron Jones, Director